

Analyst debriefing by Jason Chen, Chairman and CEO of Acer Inc.

6th Sep 2017

Jason:

To continue our story, this has been another busy season for us at Acer, there is so much to do, so little time, so to speak. First, let's take a look at the footage from the IFA GPC Worldwide Expo that concluded recently in August 2017 in Berlin.

Among the many products, one that gained the greatest number of interest is the Predator Orion 9000 desktop gaming series. Inspired by high-performance computing, it is a powerful yet incredible gaming desktop that seeks to satisfy the many serious gamers who demand faster and higher performance.

Within this gaming **rig**, it is equipped with the powerful Intel® Core™ i9 Extreme Edition processor with 18 cores, and up to 4-way AMD Radeon™ RX Vega graphics or two NVIDIA® GeForce® GTX 1080Ti graphics, that are able to support a lot of processes. Having said, an efficient cooling system becomes very important to ensure optimum machinery performance. Thus, the machine features five fans, liquid cooling and Acer's Ice Tunnel 2.0, an advanced air management solution that separates the body into several partitions, each with an individual airflow tunnel to expel heat. We are well aware of most gaming PCs has high level of DIY features, while most OEMs produce gaming notebooks. We approach this gaming desktop segment by offering a window-sided PC cases with much customisable, expandable components as we have mentioned plus RGB lighting that allow users to see through the intricacies in their **war chest**. Throughout our research, we also worked to resolve difficulties in electromagnetic interference (EMI) by adding a layer of metal mesh, another first-in-the-market technology breakthroughs for our Orion 9000 gaming series.

Swift 7 is another innovative elegance. Now I will pass on several of these latest production laptops, please touch and feel them. It is thin and light, streamline designed to show our capabilities in the field of notebook PC. We are constantly challenging our limits to come up with better and thinner products. We have raised the bar from our previous Swift 7 to further decrease the thickness below 0.98cm.

Before we proceed to another topic, let us see a video about Acer's Predator Orion 9000 and hear some of the comments from the floor at IFA Berlin. (90 seconds)

I would like to draw your attention to our range of future products. Firstly, in VR, on 18th October we will launch ACER Windows based MR head-mounted display (HMD). The first 30,000 early adopters are able to experience VR themselves in a free Ghostbuster game package provided exclusively by Sony Pictures for six months.

In terms of product segmentation, allow me to present some internal figures. We are well aware of the fact about the worldwide flattish PC sales growth and it is even in the decline. This size of bubble chart carried out by Acer Business Intelligence gives us a pictorial representation of the estimated relative market sizes, selling prices, and projected revenue growth rates of each product segments. The

products with high selling price does not always translates into high margin, but high gross profit amount. We focus on growing our market share in those segments which are expected to command high selling price and at the same time possess strong revenue growth rates into the future such as gaming PCs, the Chromebook, ultra-slim and 2-1 notebooks¹. The group is clear of our targeted market and aware of those future opportunities. The management pays great attention to ensure we divert the right amount of effort and resources into sectors identified to bring promising returns.

As a result, we achieved 27%, 91% and 68% unit shipment YoY growth for ultra-slim series, gaming PCs, and Chromebook, respectively, far surpassing the industry averages growth of 19%, 33% and 17%. We are pleased to see the rewarding payoffs in the gaming PC segment and will continue to grow this segment because it is better margin, high growth and commands a high selling price. In addition, it is low price elasticity when a good gaming machine appeals to the serious gamers in this segment. Further to that, this 91% unit growth in the gaming PCs segment is accompanied by 60% revenue growth in the first half of 2017. If you would argue that for the PC gaming segment, the rate of revenue growth does not catch up with unit shipment growth, and is caused by falling average selling price (ASP) - - the answer is yes however, this is due to the introduction of casual gaming Nitro notebook series apart from the hardcore gaming Predator series which we were doing well for the past one and half year. We will continue to launch more gaming models in 2H 2017 to cater to the mass market in order to capture a larger share and boost our revenue growth.

A recent study by NotebookCheck.net (NC) reveals that Acer clinched 4 out of 10 the most popular multimedia notebook models in the gaming industry. NC is a very established media commentator for the NB industry. We were very anxious in anticipation of this ranking release since they were first to publish their scoreboard rankings right before (Acer's) quarter result release. We are proud to see our financial results come in consistent with the public rankings.

Gadgets represents another high margin business category and it will also be our future focus apart from our core operating segments. The management pick some of our most talented staff to form an "A-team" for the design and development of gadgets. For example, when we decide to put in effort to produce 3D headset, apart from the usual comfort and aesthetic design features, we position our Galea 500 headset as another technology breakthrough, a gadget tied to VR to enable users indulge in an immersive environment and enjoy the interaction using the provided sound effect.

A transformation plan entails forming, storming and performing. During my three and half years with Acer I would say we are progressing right on the track in the performing stage. When asked by our media friends about the group's performance, my usual respond is rather straightforward -- we are constantly improving as we are not out of the woods yet and it very much depends on how fast we can run against time.

¹ 2-1 notebook encompasses the detachable and convertible notebook segments.

Good operating performance has to translate into financial figures growth. Acer experienced a minor fall of the group revenue in second quarter due to the TWD appreciation to USD about 6-7% year to date. In spite of this, the group actually recorded positive 2.3% YoY growth in US Dollar terms. The management look at this situation positively because we conduct most of our business in the overseas which is in US Dollars. Revenue figures are bolstered by improving gross margins at 11.4% in 2Q 2017, it is back to double digit again and slightly up 1.8% YoY. Furthermore, operating margin was at 1.8%, the highest in six years, as we are able to increase our revenue and reduce the operation expenses. If we look at the top line breakdowns, our major three revenue contributes from notebook, desktop, and monitor (display) segments outperforms the market with average selling price (ASPs) increased 11.6%, 12.5%, and 21.6% YoY, respectively, largely due to our first-to-market strategy, thin-and-light series, as well as gaming businesses. IDC concludes the industry's 1H 2017 worldwide PC shipment puts Acer (8.6%) in the fourth placing behind HP (22.2%), Lenovo (20.4%), and Dell (16.4%) which commands sizeable market share and ahead of other competitor brands such as Apple (8.5%), and Asus (8.0%), which are close to each other. Notably, Acer is still able to book a 4% YoY growth rate in the declining PC segment (TAM~ -1.3% YoY) as compared to other peers in the industry.

To conclude our discussion, the group have evolved from pure PC player to gaming PC, and now we are going to sustain our market position. Not only in gaming but further into VR and its related content developments – content is king. That's the IMAX part. Subsequently, we have also prepared to up an ante by venturing into AI, big data, and cloud computing services. In our many internal communication meetings, we understand that AI is a big topic, the group decided to have the right focus and grow the right segments, which are big enough to matter and small enough to win so that we are able to compete effectively.

Besides, Acer also spun off Intelligent Transportation System (ITS 智慧交通) and enterprise SI division to be more focussed on core operating activities moving forward into the future. These will be also part of our corporate transformation plan to further optimise the group's operation, with the aim to increase its operational income and reduce expense. From day 1, I was tasked to grow the group's channel and brand business. That will be my sole and premier objective. There would be more and more incubators in the process of developing channels and brands, and we are ready to push it out when a particular incubator product reaches commercial viability. Now we open for Q&A from the floor. Thank you.

Q: Jeffrey Ohlweiler, Macquarie

A: Jason Chen, Chairman and CEO, Acer Inc.,

<Q - Jeffrey Ohlweiler> The PCs market is rather stable this year. How do you describe your role in the PC market competition? Your competitor said pretty tough in US and Europe market and feel price pressure this year, what do you say in general?

<A – Jason Chen>: The PC market is highly competitive in general but we have to find our way out. There are two things in mind, first, I showed you the product segmentation chart previously, outlines the group's future focus. That is our internal "homework" so that we will be able to understand the field we are playing and able to focus and have better results. Secondly, the group will execute operational optimization via three categories, namely products, channels, and countries. We have already seen what we are going to do with our future products. Here comes the interesting point – channel optimisation will be conducted via e-commerce and conventional physical stores. We see a convergence in both sales channels. In fact, the sales number from e-commerce is coming up fast – and in between consumer and commercial, commercial products are growing (for Acer). Our commercial products take up 40% now versus consumer products 60% of total group revenue. Compared with three and half years ago, commercial was only 20% and consumer products was 80%.

There are four segments within commercial viz. education, tender, small and midsize business (SMB) and enterprise – to be honest – our growing commercial products makes 40% of the sales from the first three segments, enterprise segment itself is high margin – that's why HP easily make their 17+% gross margin while we struggle with the double digit gross margin. Although we spin-off one SI company which focus on the enterprise segment, that move explains our intention to focus, optimise, grow and further expand areas that we believe will have future growth opportunities.

Further to that, out of the many regions and countries, what is super tough market? US market is identified as a good market and Acer is doing well. Pan Americas is extremely market. Latin America is a broad area for us, and we are very happy with our performance in Latin America. In Brazil, we are number ONE in terms of unit and value. In Canada, we are always at first or second position for a long time, in competition only with Apple products. In Mexico, we are number TWO. In Columbia, Argentina, and Ecuador, we are all growing, as we are very small base there. Asia Pacific has been our strength all except China, where its market is hyper-competitive. There is also many disruptions and different factors happening in the China market. It is tough for us because it is the home turf of some market players, not just one but of many other (brands) as well. We still have room to do in China. Other countries like Malaysia, Indonesia, Thailand, Philippines, we are number ONE for eons I don't remember for how long, both in terms of units and value. We are always doing very well there in those countries. For Europe, we are well, Russia deserves special mention. (Sales in) Russia has been "falling asleep" at the height of their currency crisis, you practically can't do business there. Fortunately enough, our footprint in Russia is very, very good. During the Ruble crisis, we decided to hold on our breath and did not retreat. We analysed the country's economic situation and determined that it is a short term problem and not structural issue. When the market turned around, we are ready to jump right back into business action. So now Acer is number ONE in Russia and are profitable. We are again very happy with our results in Russia. What are the three countries in Benelux? In Belgium, Netherlands and Luxemburg we have only one office but Acer is number ONE there, all three countries add up together. Conventionally, we have been doing well in the UK, France, and Germany, however,

the challenge this year has to be fluctuation in US Dollar caused by the new Trump administration, making business environment much harder to manage, which is a universal fact. In India, we are recovering because there's lots of reform led by the Indian government of which (policies) are pretty much confirmed. I think the (Indian) market is more stable and we are able to perform much better from now.

<Q - Jeffrey Ohlweiler>: The PCs market down about 35% in past five years from the peak. What do you think about the PC market next five years, stable or decline? Structure or ...?

<A – Jason Chen>: As a player in the industry, we are not in the position like you to analyse the market sentiment – wait and see how the market is doing. Our job is to stimulate demand and grow the market. We believe the only way to do so is by creating innovation and providing good technology – give people strong reasons why you should buy (Acer's products).

Q: Angela Hsiang, KGI

A: Jason Chen, Chairman and CEO, Acer Inc.,

<Q - Angela Hsiang, KGI>: Could you share with us the revenue and shipment contribution from Acer's gaming products?

<A – Jason Chen>: I give you three numbers: mid-single digit in terms of unit shipments; approaching double digits in 2Q 2017 from high single-digit in 1Q 2017 in terms of revenue; gross margin contributes high-teens (less than 20%) of total figure.

<Q - Angela Hsiang, KGI>: The group sales was up 2-3% YoY in USD terms with the gaming revenue grows 60% YoY in 1H 2017. What percentages of these focus products will act to help Acer group revenue or profit?

<A – Jason Chen>: At Acer, our notebook PCs are based on three major categories: thin-and-light, gaming and conventional PCs. We have been talking about thin-and-light and gaming but how about conventional PCs? Since the whole conventional PC segment is in decline, our conventional PC declined faster than the industry. According to IDC, Acer sustained 4% growth YoY in PC shipment in the first half this year versus total addressable market down 1.3% YoY. We will grow areas that we discover values.

How do we expand growth? First we need to understand the underlying meaning of growth. We will achieve that by value creation growth and not pure revenue growth, which will soak up much capital, resources and manpower in the pursuit of the latter. We quantify value creation by the improvement in gross margin [or gross profit]. When Acer acted as a brand dealer, Acer suffered low gross margin [6+%] for couple times. We have successfully increased the group's gross margin from 6% three years ago to 11.4% in 2Q 17. This is value creation. Gross margin improvements is more important than revenue growth.

Q: Kevin Chang, Fubon

A: Jason Chen, Chairman and CEO, Acer Inc.,

<Q - Kevin Chang, Fubon>: In terms of management structure, are you able to execute your strategies smoothly as the CEO? What is the restructuring (transformation) progress in your company. Have you clean out your balance sheet, ex. Subsidiaries investment? Will there be any negative surprises later to the street?

<A - Jason Chen>: I am fully delegated and empowered as the CEO by the board of directors. I gain full support from the board and we have consensus. But I am not naive. CEO maintains good relationship and healthy informational exchange with the board of directors.

At the same time, Acer has very clear lines of business (LOB) in the organisation. There are two main divisions in principle – headquarter (HQ) operations and regional operations (RO). For example, HR, finance, and legal department are grouped under HQ operations. The many country offices are grouped under three geographic regions as Pan-America (PA), EMEA and Asia Pacific (AP). I spent more than a year to understand all the BU heads capabilities. It is more stable now. To be honest, we did “reorg” (corporate reorganisation) in the very first year of my tenure as CEO of the company and there’s no need for restructuring now.

I have told the new CFO that I will focus on the balance sheet part going forward. We will seriously consider any future possible M&A activities to rebuild the group’s line of business. Apart from my usual day-to-day job, we seek to grow the group’s market capitalisation, which is my KPI. Except looking at profitability, P/B and P/E figures, I also want to make sure the group is on the right track using the right technologies. I make a habit to review the group’s rolling six months income statement forecast every week. Until now, I have some ideas of the group’s operational expenses, headcounts, and sales campaign. On the balance sheet, we will lower down the cash level and reduce our debt ratio.

<Q - Kevin Chang, Fubon>: Is there any technology barrier that Acer could sustain in the gaming PC? It is expected to become a Red Ocean for the gaming industry next year. How long will Acer maintain your position?

<A - Jason Chen>: I came from semiconductor industry and know that all of the PC features utilize the same CPUs and GPUs. I think differentiation will be the leading thermal solution on the PC systemic level, because good heat dissipating system enables chipsets performance and unleashes its maximum efficiency. We were the first to introduce metal fans and LiquidLoop™ (fan less). We take lead of patent filing and will continue to do so to sustain our market leadership of thermal. To add to my point, when most brands boast their slim notebooks (for those with thickness below 2cm.), they do not incorporate the mechanical keyboard, which is an important feature for hardcore gamer. Many brands also fail to optimise their computing performance due to overdrive issue as they do not have the thermal cooling system. There are some underlying truths that lead us to top the ranks among the peer reviews in the PC gaming industry. Therefore we are very confident in our technologies and products.

I strongly believe in these critical details that will set us apart favourably in the long run.

Is there another red ocean ahead for us in the gaming PC industry? It depends on markets and regions. China is the hyper-competitive and the biggest market. Like it or hate it, just the way it is. We will have to deal with it. We possess the differentiation lead by having both the low end models and premium high end models, such as Predator 21X (NB), Triton 700 (slim NB), and Orion 9000 (Desktop). We understand the entry level PC market is hyper-competitive. We prepared for that, as Acer has the lowest operating expense among the peers.

Q: Melrose Chiu, Morgan Stanley

A: Jason Chen, Chairman and CEO, Acer Inc.,

<Q - Melrose Chiu>: Acer has been doing quite well recently with its range of new products, how do you comment on Acer's overall direction in terms of product mix and services five years from now?

<A - Jason Chen>: There will be no absolute answer for your question. No one is able to accurately forecast the trend of market six months thereafter because market cycle is dynamic. It evolves very fast. As the group embark on a journey of optimisation improvements, our priority is still value creation. We will first look at the prospect of each items when we conduct product segmentation, and determine in which product segments that we are able to create values. If enterprise is profitable, which I am so sure, we will grow the enterprise business with Taiwanese businessmen.

Many parties from the board of directors, media, and internal staff are equally concerned where the company is heading to, we already have a crystal clear corporate strategy. Acer used to be a brand house. Moving forward we will emulate the House of Brands model and achieve success like P&G. P&G carries many different brands under its umbrella with n-number of products. In three to five years of time, we strive to work towards creating many different products carrying different names in what is known as the hybrid model. Currently, PC products that carry the Acer brand takes up about 80% of total revenue, we will be creating new brands and new businesses – how many? As many as possible. With all these in mind, PC business will still be our bread and butter and will not be side-lined. We will continue to optimise core business consistently and at the same time grow new businesses up to a stage it is viable. After that, they will be up and running by their own with independent brand names, management, service operations and even office layouts. For example, if Pawbo achieves critical mass it is going to attract pet feed companies talking to us. These companies are interested in the amount of data it collects on the web using IoT technologies. These are the group's future direction, to grow many businesses in different industries using IT technology.

Q: William Yang, Citigroup

A: Jason Chen, Chairman and CEO, Acer Inc.,

<Q – William Yang>: What is your opinion on Windows-on-ARM application? What are the potential opportunities or threat from the Wintel – how it will act to affect Acer.

<A - Jason Chen>: First I need to clarify there's no on-going "Windows-on-Arm" (WoA) project within Acer². The fundamental objectives in WoA are built-in LTE enable (always-connected) and have a longer battery life. We have no power over what is happening between Microsoft and ARM. In Acer, we have the solution for always connected, for example, Swift 7 with LTE enabled technology is also the thinnest and thermal efficient model in the NB market.

If no any further questions. We thank you for your time and effort participating in this session at Acer Xizhi office.

² Windows-on-Arm is a version of Windows 10 that will run on ARM hardware.